INTL-0439-90 Br:2 VMark

Allan Bernstein, Baltimore District

Phyllis E. Marcus, Chief, Branch 2, Office of the Associate Chief Counsel (International) CC:INTL:2

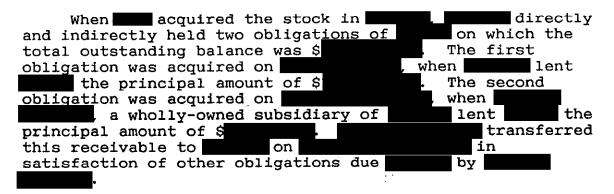
THIS DOCUMENT INCLUDES STATEMENTS SUBJECT TO THE ATTORNEY-CLIENT PRIVILEGE AND THE ATTORNEY WORK PRODUCT PRIVILEGE.
THIS DOCUMENT SHOULD NOT BE DISCLOSED TO ANYONE OUTSIDE THE IRS, INCLUDING THE TAXPAYERS INVOLVED, AND ITS USE WITHIN THE IRS SHOULD BE LIMITED TO THOSE WITH A NEED TO REVIEW THE DOCUMENT FOR USE IN THEIR OWN CASES.

This memorandum is supplemental to our memorandum of May 7, 1991, which discussed issues raised under section 956 of the Internal Revenue Code with respect to

FACTS:

For convenience, we have restated the facts of this case. On _______, a domestic corporation, purchased all of the stock of _______, a made a section 338 election with respect to this purchase and selected as the deemed acquisition date for purposes of this election. At the time of this acquisition, ______ owned all of the stock of _______, a U.K. corporation, which owned all of the stock of _______, a domestic corporation. In ______, direct ownership of ______ was shifted from pursuant to a plan of reorganization.

¹ Section 224(d) of the Tax Equity and Fiscal Responsibility Act of 1982, as amended by section 306(a)(8)(B)(i) of the Technical Corrections Act of 1982, provided guidelines under which a purchasing agent could select a date that would be treated as the acquisition date for purposes of making a section 338 election under the transitional rules of section 224(d)(2).



ISSUE:

Does 's election under section 338(g) of the Code with respect to affect whether the obligations that held are "United States property" within the meaning of section 956(b) of the Code?

LAW & ANALYSIS:

Section 956(b)(2)(F) excludes from the definition of United States property, the stock or obligations of a domestic corporation which is neither a U.S. shareholder of the controlled foreign corporation (CFC), nor a domestic corporation, 25% or more of the total combined voting power of which, immediately after the acquisition of any stock in such domestic corporation by the CFC, is owned, or considered as being owned by such U.S. shareholders in the aggregate.

Section 1.956-2(b)(1)(viii) of the regulations, provides that the stock or obligations of an unrelated corporation will be excluded from the definition of United Sates property. An unrelated corporation is a domestic corporation that is neither a United States shareholder of the CFC making the investment, nor a corporation 25 percent or more of whose total combined voting power is owned or considered as owned (within in the meaning of section 958(b)) by United States shareholders of the CFC making the investment. Section 1.956-2(b)(1)(viii). The determination of whether a domestic corporation is an unrelated corporation is made immediately after each acquisition of stock or obligations by the controlled foreign corporation. Section 1.956-2(b)(1)(viii).

Section 1.956-2(d)(1) of the regulations provides that property shall be considered acquired by a foreign corporation when the corporation acquires an adjusted basis in the property.

The taxpayer takes the position that section

956(b)(2)(F) of the Code and section 1.956-2(b)(1)(viii) of the regulations require the test for relatedness, which determines whether the obligations are U.S. property, to be made when first acquired an adjusted basis in the obligations before became a CFC. At that time was not a related corporation under section 956(b)(2)(F) and therefore the obligations would be excluded from the definition of U.S. property. While we do not agree with the taxpayer's interpretation of section 956(b)(2)(F) and the regulations thereunder, as discussed in our prior memorandum, the taxpayer's argument is in any case irrelevant for tax years of beginning after the section 338 election.

Section 338(a) provides that if an election under that section is made, the target corporation will be treated as having sold all of its assets at the close of the acquisition date² at fair market value in a single transaction, and shall be treated as a new corporation which purchased all of the assets of the old corporation as of the beginning of the day after the acquisition date.

became a CFC when it was acquired by ... on ... As a result of the section 338 election, acquired a new adjusted basis in all of its assets, including the ... obligations, as of the beginning of the day after the acquisition date, ... Accordingly, section 1.956-2(b)(1)(viii) requires the test for relatedness to be made on ... On that date ... On the U.S shareholder of ... owned more than ... of the total combined voting power of ... The obligations therefore are "U.S. property" for purposes of section 956 for the taxable years of ... beginning after

CONCLUSION:

As a result of the section 338 election, acquired a new adjusted basis in the constant obligations on the day after its constant deemed acquisition date. At that time, was a CFC and constant was a related corporation under section 1.956-2(b)(1)(viii) of the

The date selected as the acquisition date under the transitional rules will be the acquisition date for purposes of section 338(a). P.L. 97-248, section 224(d)(5)(A)(i), as amended by section P.L 97-448.

regulations. Accordingly, the law is clear that as of the to the control of the c

If you have any questions about this memorandum, please call Valerie Mark at FTS 566-6645.

cc: Jack Doherty
Judy Miller